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TRADE AND DEVELOPMENT BOARD
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Expert Meeting on Ways to Enhance the Production and Export Capacities of
Developing Countries of Agriculture and Food Products, Including Niche Products,
Such as Environmentally Preferable Products
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# WAYS TO ENHANCE THE PRODUCTION AND EXPORT CAPACITIES OF DEVELOPING COUNTRIES OF AGRICULTURE AND FOOD PRODUCTS, INCLUDING NICHE PRODUCTS, SUCH AS ENVIRONMENTALLY PREFERABLE PRODUCTS

**Background note by the UNCTAD secretariat**

**Executive Summary**

International trade in food and agricultural products offers significant export opportunities to developing countries. Exploiting these opportunities is especially important for many of these countries, in particular African countries and LDCs, because agriculture is the mainstay of their economies. Success, however, is not easy. World markets are increasingly competitive and exigent, with a multitude of standards to be met. Skills required in both production and trade are becoming more and more complex. This is true for both the public and the private sectors. In most cases, their upgrading necessitates international cooperation. Moreover, many agricultural products face high tariffs and/or non-tariff measures. Comparative advantage, which often rests with developing countries, is not always allowed to determine trade patterns. Rapid demand growth for organic food in developed countries is likely to create temporary supply-demand gaps, of significant magnitude at times, that can be bridged by supply from developing countries. Such short-term opportunities can, however, only be seized if certification requirements in export markets can be met and market access is facilitated. As long as developing country producers retain significant production cost advantages, based on lower labour costs or natural production factors (such as a longer vegetation period that allows several harvests), they might be able to consolidate market shares gained in the short term.

This note does not aim to provide an extensive analysis of all the issues involved, but to identify important issues that could be addressed by experts participating in the meeting.

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## I. INTRODUCTION

1. The mandate for this Expert Meeting stems from two sections in the Plan of Action, adopted by UNCTAD's Tenth Session: "Strengthening Supply Capacities in Export-oriented Sectors of Commodities" and "Trade and Environment". According to the Plan of Action, UNCTAD's work on commodities should among other things focus on "Identifying ways to improve the supply capacity of commodity-producing countries, as well as obstacles hampering the development of processing industries and assisting commodity-dependent countries on how to fully exploit commodity diversification as a major potential avenue to industrialization." (Paragraph 144). Furthermore, UNCTAD's work on trade and environment should among other things focus on "supporting developing countries' efforts in promoting production of and trading opportunities for environmentally preferable products." (Paragraph 147).

## II. TRENDS IN WORLD TRADE IN FOOD AND AGRICULTURAL PRODUCTS

2. As a result of improvements in productivity, food production increased in all regions over the past decade. The rate of increase in production was higher in developing countries than in developed ones, although a considerable portion of the increased production in the former group of countries was consumed domestically. World agricultural exports[1] increased at an average annual rate of 3.2 per cent in value terms from 1990 to 1999, with food exports[2] growing at a rate of 3.7 per cent. It should be recalled that food prices declined by close to 20 per cent during the same period[3] and that world food trade therefore showed a healthy rate of growth in volume terms, particularly since trade in agricultural products was less subject to the "double counting" that has influenced the statistically registered growth rate of trade in manufactures.[4]

3. Food exports from developing countries increased at a higher rate during the decade, or by 5.6 per cent per year on average, than those of developed countries. The fastest food export growth occurred in the African region, almost doubling in value between 1990 and 1999. However, high rates of export growth were concentrated in a minority of developing countries, particularly in those with products such as fresh fruits and vegetables, for which demand has grown rapidly. It should also be noted that the relative rapid rise in the food exports of developing countries followed several decades of falling export shares for agricultural products from this group of countries. Moreover, developing countries continue to account for a relatively small share of world exports of processed food products. Therefore, they have not been able to reap great benefit from the fast growing trade in these products, which also brings down their share in total trade in agricultural products. Several factors have influenced trends in international food trade over the past decade, including, in particular, the following:

- Trade liberalization and reduced government intervention in developing countries;
- Continued support to domestic agriculture in developed countries;

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1 SITC numbers 0, 1, 2 (except 27, 28, 233, 244, 266, 267) and 4, figures from the database of the United Nations Food and Agricultural Organization.

2 SITC Rev. 2 numbers 0, 1, 22 and 4.

3 The UNCTAD index of free market prices for food in US dollars fell from 123 in January 1990 to 100 in December 1999 (1985=100), UNCTAD, Monthly Commodity Price Bulletin.

4 As manufacturing has become more international over the years and different stages of processing increasingly take place in different countries, the "double counting" of manufactures trade due to the adding up of trade in, for instance, cars, vehicle parts and internal combustion engines, has increased.

- Shifts in the composition of demand, arising from changes in taste, consumer concerns in the area of food safety and quality, and increasing incomes,
- Changes in industry structure

4. The increase in developing country agricultural production and exports can be partly attributed to policies, including deregulation, aiming to stimulate supply. As has been noted, such policies may have contributed to the improvement in farm gate prices as a proportion of export prices in many developing countries.[5] At the same time, however, the retreat of Governments from activities intended to support the farming sector, including the abolishment of many of the functions of marketing boards or of the boards themselves, reduction in extension services and deteriorating access to credit for small farmers, has limited any progress made. Moreover, since barriers to agricultural imports have been abolished or dramatically reduced in most developing countries, producers in these countries are facing increased competition from imports. Accordingly, developing country imports of agricultural products have increased, particularly in Latin America and Asia. Food imports in Latin America increased at an average annual rate of almost 8 per cent during the 1990s. In Asia, an even stronger import growth of 11 per cent per year between 1990 and 1996 was cut short by the Asian crisis. By 1999, in spite of the subsequent fall in developing country imports, developing countries accounted for more than 26 per cent of world food imports, compared to approximately 21.5 per cent in 1990. Thus, the increase in exports has been matched by an equally large or larger increase in imports in all developing regions, which illustrates the conditions of more intense competition facing developing country producers.

5. In developed countries, support to agricultural production and exports has more than offset the competitive disadvantage caused by their higher labour costs and has almost succeeded in maintaining the share of these countries in world food exports over the last decade. On average, farmers in the European Union, Japan and the United States received a $20,000 of support in 1998 and subsidies accounted for 40 per cent of gross farm receipts in 1999. Developed countries have been particularly successful in maintaining and increasing their market shares for processed products. From 1980 to 1996, the average annual rate of growth in OECD country exports of primary agricultural commodities was 2.5 per cent, while that of processed agricultural commodities was 6.5 per cent.[6] The latter group includes products requiring significant blending, processing and marketing activities.

6. Changes in the composition of demand have been particularly important for food products. In developed countries, the consumption and trade of high-value products such as fresh fruit and vegetables and certain niche items, such as organically grown products, is increasing rapidly. In developing countries, as incomes grow, the pattern of food consumption is also changing, leading to increased demand for "high-value" products such as vegetable oils and meat, for which demand in developed countries is stagnating.

7. Confidence in food quality has been challenged in recent years by various food scares and health concerns, such as Bovine Spongiform Encephalopathy (BSE) in cattle and its link to variant Cruetzfeldt Jacob Disease in humans. As a result, consumers expect retailers to supplement, through their purchasing practices, Government measures for ensuring food safety. The competition among retailers therefore increasingly involves food safety aspects.

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[5] UNCTAD, Trade and Development Report, 1998, p. 162.

[6] Figures in this paragraph are from OECD, Agricultural Policies in OECD Countries: Monitoring and Evaluation, 2000 (Paris, 2000).

Consumers are also demanding more transparency, tractability and assurance in the food chain. It is important to note that the quality requirements of firms that import food products into the major markets of industrialised countries are, at times, stricter than those legally required by Governments. Meeting these requirements is a significant challenge for developing country firms aspiring to enter global value chains of food products and other agricultural products.

8. In many developed countries, significant gaps exist or are likely to emerge between demand and domestic supply, notably in organic food, particularly in the short-term. This might allow developing country producers to acquire and expand significant market share in developed countries. In the United Kingdom, for instance, it has been reported that demand for organic foods is increasing by 40 per cent annually, whereas domestic supply is expanding by 25 per cent only.[7] Imported products now account for 75 per cent of organic sales. In the United Kingdom, 80 per cent of organic fruit and vegetables are imported.[8] Developing countries might profit from such demand, because traditional farming practices, that apply soil building and either use very little agro-chemical inputs or none at all, are widespread. Although not certified as such, these practices often are *de facto* "organic".[9] Generally, there is also an abundant supply of labour and many local communities have a rich body of traditional knowledge related to farming practices. This gives many developing countries a comparative advantage in growing organic products.

9. Fundamental changes in Government policies toward conventional intensive agriculture and animal husbandry seem to be under way in many developed countries.[10] Several Governments have recently announced ambitious plans to promote organic agriculture.[11] However, the question in this regard is: What policy tool kit will be employed and will it have trade distorting effects?

10. The manner in which the commodity chains are organized has undergone significant change, from production in exporting countries to the retail level in consuming markets. The common denominator at all stages of the chains is closer integration of international trade and production through the penetration of large transnational production and distribution companies, including supermarket chains, into the agricultural supply structures of both developing and developed countries. A few decades ago, the dominance of large companies in the world commodity economy was principally through their actions on international markets. Now, increasingly, it is also through their direct influence on what is produced and how. At the international level, there is a continuing concentration of trade and vertical integration of large firms at the international level. At the level of commodity-exporting developing countries, liberalization has led to the appropriation of trading networks, both

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7 Various press releases at BIOFACH Trade Fair, Nürnberg, Germany, February 2001.

8 Conversely, in Germany, 85 per cent of demand for organic products is met by domestic supply.

9 In India, for instance, 70 per cent of the arable land is mainly rain-fed and fertilizers have not been used. Similarly, it is estimated that about 10 per cent of the cultivated land in Brazil uses methods of "alternative" agriculture.

10 Agenda 2000 of the European Union, for example, already contains some economic incentives for extensive modes of production. For more information, see: Statement of Mr. Fischler, European Union Commissioner for Agriculture before the European Parliament (speech 01/65), Strasbourg, 13 February 2001.

11 For example, the Government of Germany recently announced plans to ensure that organic agriculture will obtain a 20 per cent market share within 10 years. Statement by Renate Künast, German Minister for Consumer Protection and Agriculture on 8 February 2001 (see: www.bml.de).

domestically and for export, by foreign firms and the penetration of national markets by imported products, often through foreign-owned supermarkets. In the retail markets of developed countries, finally, the most important change has been the growth of supermarkets, which has led to the near elimination of independent traders and increased importance of brand name recognition.

## III. CONSTRAINTS TO INCREASED PRODUCTION AND EXPORT BY DEVELOPING COUNTRIES

### A. General constraints

11. Access to developed country markets remains an important, or possibly the most important, constraint to the expansion of developing country agricultural exports. Continued agricultural trade liberalization is thus a prerequisite for increased developing country exports. However, since the Expert Meeting is intended to focus on ways to enhance the supply capacities of developing countries, the present note concentrates on constraints that are amenable to actions that can be taken by developing countries themselves. Such actions obviously stand a greater chance of success under improved market access conditions.

12. Limits on access to information and on access to finance are two very broad categories of constraints from which are derived almost all other types of constraints. Access to information about regulatory requirements, prices, demand, quality factors, pricing and marketing practices and logistics is of crucial importance at each stage of the production and processing chain. Developing country producers are almost always, without exception, at a distinct disadvantage in this respect. During discussions at regional and sub-regional workshops organized by the UNCTAD secretariat during 2001 in connection with a project under the United Nations "Development Account"[12], it has repeatedly been noted that developing country producers, particularly small farmers, suffer from lack of information about consumer preferences and market conditions of strategic importance. This limits their ability to determine which are their own competitive advantages and to identify market segments in which they could be successful. When it comes to information of a regulatory or quasi-regulatory nature, such as environmental standards or labelling requirements, the difficulties faced by small developing country producers are even more evident and remain highly significant even for formal or informal groups of producers. While the information deficit can be partly alleviated by forming cooperative arrangements with larger, foreign-based partners, such arrangements do not render the playing field level and the developing country producer is still at a disadvantage.

13. Access to finance has become a more crucial constraint with the dismantling or downgrading of marketing boards in most developing countries since these boards often provided credit to farmers. Commercial credit is usually not available to large parts of the farming sector, particularly small farmers. While several Governments and private sector organizations are attempting to fill the gap through the introduction of innovative modes of

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[12] The project, which deals with diversification and commodity based development, has as its main objectives: (i) to promote the horizontal, vertical and geographical diversification of production and trade structures; (ii) to improve Governments' capacities to formulate focused, effective and sequenced policies in this respect; (iii) to increase the competence of enterprises in adapting their business strategies and supplies to the Post-Uruguay Round trading framework; and (iv) to strengthen positive linkages between the commodity sector and the rest of the economy.

structured finance, these promising initiatives have not yet affected the bulk of developing country agricultural production. Two other developments have also raised financing needs. First, the need to comply with standards, both those contained in intergovernmental or national legal instruments and those imposed by private sector bodies or individual importers. These standards place many smaller exporters under severe financial pressure, since meeting the standards necessitates major investment expenditures. Second, the investment necessary in marketing, particularly in building brand name recognition, usually exceeds the financial resources of individual developing country exporters and of associations formed by such exporters.

14. An important precondition for developing country export expansion is the availability and effective dissemination of new technologies and means of production that allow developing country producers to fully profit from their comparative advantage. It is particularly important for developing country producers to be assured of access to seeds from improved plant varieties resulting from technological development. For this reason, it is also important for developing countries to maintain an independent capability to carry out agricultural research and development work.

15. As noted earlier, reductions in extension services have taken place in many developing countries, usually as a result of budgetary exigencies. In many cases, however, these reductions have placed severe limits on the growth in agricultural production and exports, particularly from small farmers. Lack of or deteriorations in physical infrastructure, both with respect to transport and storage, have resulted in additional constraints on growth which have to be eliminated if investments in productive capacity are to yield the hoped for results.

### B. Constraints for organic and other niche products

16. Conversion to organic farming may be hindered, for instance, by lack of awareness of organic farming systems, managerial costs, risks of shifting to new farming methods, lack of infrastructure, lack of marketing facilities, limited access to capital, and inability to capture economies of scale. Developing country producers also have to secure the minimum required nutrients to crops only from organic sources and sufficient amounts of organic matter as well as organic fertilizers. In addition, as in developed countries, the competitiveness of organic products in developing countries is adversely affected by the fact that environmental costs and benefits are, in general, not "adequately" reflected in price.

17. Constraints to increased exports of organic products from developing countries include high certification costs, lack of market information and marketing strategies, insufficient export facilitation, complex procedures in importing countries, and tariff and non-tariff protection in import markets. Furthermore, traditional agriculture that has been practised for centuries, does not receive appropriate recognition in developed country markets.

18. Certification and accreditation issues play a particularly important role. In most cases, developing country exporters depend on certification by international certification bodies to be able to market their products as organic in foreign markets. Costs of certification vary, but

can be significant.[13] Small developing countries, in particular LDCs, may find it difficult to set up a national certification infrastructure. Their efforts to reduce certification costs could focus on attracting donor support and development projects. In Madagascar, for example, certification costs have been borne by international certifiers.[14] Developing countries could also encourage international certification bodies operating in their territory to train and employ local personnel and use local inspectors. Where organic production becomes relatively more important, there will be a larger need to develop domestic standards and create domestic certification infrastructure. National standards can also contribute to the creation of domestic niche markets, as occurred in Brazil. In addition, international accreditation by developing country certification bodies should be relatively easy and affordable. The International Federation for Organic Agriculture Movements (IFOAM) Accreditation Programme provides for accreditation of certifiers on the basis of their "Basic Standards" and "Criteria for Accreditation". Developing countries with a relatively large organic sector and a standards and certification structure in place, can negotiate equivalency agreements with other countries. In practice, however, insufficient progress has been made in this respect.[15]

19. Many environmentally preferable products, including organic produce, are subject to the tariff and non-tariff restrictions faced by conventional products in developed country markets. Import quota and tariff-rate quota systems, such as in the case of fruit that competes with Northern supplies, can be a serious handicap for expanding market shares in developed countries.

## IV. QUALITY AND PRODUCT DIFFERENTIATION ISSUES

20. The exigencies of consumers necessitate a very high degree of professionalism in today's international market place. To compete in the international market, the supplier offers not just a product, but a range of services, which include approved quality systems, a degree of assurance about continuity of supply and the capacity to bring new products and product presentations to market rapidly. Quality, in the current context, refers not only to the characteristics of the final product but also to the way in which the product is produced, processed and transported.

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13 Certification is not a one-time procedure, it is carried out continuously on the basis of ongoing monitoring and inspection. The costs vary. At farm level, it is generally a fixed amount, calculated from the number of days required for inspection. Certification is often conducted by Northern organizations, partly drawing on local inspectors and, according to some UNCTAD studies in India and Viet Nam, can account for as much as 5-30 per cent of farm gate prices (UNCTAD studies as part of projects IND/99/965 and VIE/98/036, forthcoming). See also: Myers, D. and S. Stolton, Organic cotton, London, 1999, p. 97). For processors and traders, there may be a fixed price, as well as a percentage of the commercial value ranging between 0.3 per cent and 1 per cent. ITC, op cit. p. 11.

14 UNCTAD, Le commerce international et la protection de l'environnement a Madagascar, Analytical Studies on Trade, Environment and Development, No. 2, Geneva, 2000.

15 Article 11 of Regulation 2092/91/EEC should open the European Union organic food market for products from third countries, based on the concept of equivalence. However, only six countries (with certain inspection bodies named) are on the list: Argentina, Australia, the Czech Republic, Hungary, Israel and Switzerland. European Union Council Regulation 2083 of 1992, introduced a case-by-case import permit procedure as an alternative way to access the European Union market for organic food products. The case-by case procedure, which applies to every consignment imported from a non-listed third country, was set up as a provisional measure, but has remained in force.

21. Quality assurance that used to be provided by Government controlled bodies such as marketing boards is no longer available in many developing countries where such institutions have been abolished. One way in which the developing country firms are trying to meet quality challenges is by adopting their own voluntary standards and codes of conduct. Moreover, control by firms that purchase their products is more and more practised.

22. International trade relationships are affected by quality interpretation. Defined under various legislative instruments, the term "quality assurance"[16] primarily refers to health and safety issues. Everyone involved in food production, processing, distribution and retail is called upon to observe "due diligence" to ensure food safety (Howells *et. al.* 1998). In practice, suppliers must demonstrate that they have a quality assurance and appropriate control system. Many firms have developed private quality standards, which are promoted by trade organizations or are self-regulated, whilst others are independently certified. An independent body undertakes the certification procedure, involving setting of standards and establishment of the monitoring process.[17] In most cases these bodies reside in industrialized countries and their services are rather costly, especially for firms in developing countries. Consumers also request information on how food items are produced[18] and demanding that production follows certain accepted principles. Examples include, among other things, organic food and vegetables and other fair trade and ethical products.

23. Requirements set by regulatory authorities in different countries are frequently diverse and confusion may exist over what is being assured and on what basis. What may be considered by some to be product differentiation on food safety grounds, may be considered by competitors to be another form of trade barrier. It is the function of Sanitary and Phytosanitary (SPS) and Technical Barriers to Trade (TBT) agreements to establish rules and promote transparency in this respect. In many instances, however, "private" requirements of importing firms, which generally reflect consumers' preoccupations are the binding constraints for producers and exporters.

24. As a global approach covering, in a coherent manner, the specific requirements of national, regional and international markets regarding quality standards, does not exist, companies are inclined to adopt the ISO 9000 and ISO 14000 series of standards. Moreover, the internationally accepted Hazard Analysis Critical Control Points (HACCP) principles provide guidelines for the implementation of quality systems in the food chain. As these can be considered common elements of most quality standards, their implementation by producing firms could go a considerable way in meeting many standards. In fact, one approach[19] of streamlining quality considerations could be integrating the requirements for food quality and environmental management into one system based on existing internationally recognized management standards such as ISO 9000, ISO 14000 and HACCP.

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16 Juran, J.M., (1989). *Juran on leadership for Quality – An executive handbook*. The free press, New York, USA. 368 pp – included the consumer into his concept of product quality. His definition "quality is fitness for use" means "quality is to meet the expectations of the consumer".

17 For more information, see UNCTAD, Profiting from "green consumerism" in Germany - Opportunities for developing countries in three sectors: Leather and footwear, textiles and clothing and furniture. No. 1. Geneva, 1999.

18 See Michael Bochlje, Lee Schrader and Jay Akridge in *"Observations on Formation of Food Supply Chains"*. Department of Agricultural Economics, Perdue University, 1998.

19 This refers to a model for environmental & food quality assurance outlined by Barnes & Davies, in Quality Assurance in International Food Supply, Royal Agricultural College, Gloucestershire, GL7 6JS, 1998, U.K.

This approach could, however, require investment that would be difficult to finance for small producers. In any case, these have already been adopted in the main importing countries, such as the United States, Japan and the European Union. HACCP, based on hazards and risks analysis, is at the core of the SPS Agreement through explicit reference to the international standards, guidelines and recommendations of the Codex Alimentarius Commission which has adopted HACCP as the international standard for food safety.

25. Investment needed to bring a company up to the standards of ISO 9000 and ISO14000 or a HACCP plan can be substantial. As such, enterprises, especially in developing countries, are unable to face such costs. In the case of the fish industry in Latin America, for example, the cost of upgrading the installations and processing facilities to meet HACCP requirements is estimated at $300,000 per company. The managerial requirements stemming from the implementation of these standards also create important difficulties for developing country exporters. Earlier, production according to the regulations of the producing countries, not surpassing the residue thresholds and satisfying other quality and safety requirements was sufficient. Now, the whole production process, not only the final product, becomes the subject of scrutiny and the standards to be followed may be set by the importing countries or companies. In 1999, for example, Japan urged meat-exporting countries to certify meat exports as having been processed using equivalent or higher sanitation standards than Japan's. Before, rules required meat exporters to certify that their products had been processed in line with the exporting countries' rules.[20]

26. Product differentiation is one of the strategies adopted by firms to tap opportunities offered by the changes in food habits, especially in developed countries. High-income consumers tend to be less price sensitive and more willing to pay for quality, variety and convenience. However, neither quality requirements nor tastes are the same in every market. In fact, perfectly safe, tasty and nutritious products are sometimes excluded from the markets of industrialized countries owing to their appearance alone. Exporters can increase their earnings by successfully directing different grades of products to different markets. For example, many different cuts can be prepared from one chicken each facing a strong demand in some market. Moreover, even lower quality products can find utility in processed items so long as they fulfil safety requirements.

27. Naturally one important means for product differentiation, particularly for processed products, is branding, including the use of geographical indications, if recognized by consumers. A number of recent successful marketing campaigns have demonstrated that psychological attributes are used to create specific market niches even among bulk products, such as tropical beverages. "Gourmet coffee", for instance, is sold in special coffee shops with a certain atmosphere and image, leading to what might be termed "de-commoditizing of commodities." Consequently, the importance of expenditures on advertising and related activities is increasing. This puts developing country traders at a disadvantage and contributes to the concentration in the commodity economy. Difficulties are almost insurmountable for developing country exporters to differentiate their products and establish new brand names to compete with the existing globally accepted ones.

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[20] Bridges, Vol. 3, No. 35, 6 September 1999.

## V. SPECIALITY AND OTHER NICHE PRODUCTS

28. Large vertically integrated firms and supermarket chains dominate the value chains of mainstream food commodities. In order to appropriate at least some of the sizeable value added generated at the marketing and distribution stages, independent developing country exporters would have to identify speciality and niche products for which markets are smaller and the scale economies of the large companies are not very important in determining competitiveness. The main candidates for niche markets include exotic fruit and vegetables as well as ethnic products. The increasing incomes, education levels and tourism activity have contributed to the widening of consumer tastes to accept such products. Organic markets also offer new opportunities, which are examined at greater length.

29. Increasing the volume of sales is often a primary objective of enterprises. Putting the niche product on supermarket shelves, is one important avenue for achieving this. However, the more sales are increased, the less the product maintains its niche character. As a consequence, the premiums associated with this are reduced. Kiwi fruit, which has become a mainstream fruit from its origins as a niche product, is an excellent example in this respect.

30. Certain horticultural products from developing countries have maintained their niche character over the years. Fine green beans, babycorn and mangetout, which secure much higher prices than the traditional varieties of beans and peas are examples of such products. Although they do not face competition from producers in the importing countries, the income obtained by producers in the developing exporting countries still represents a minor proportion of the final price owing to the large margins of distributors and retailers in import markets. Naturally, the more processing takes place in the developing countries, the higher are the returns. This is the case even when the processing is a rather simple operation as drying or packing.

31. Other initiatives underway for the development and the expansion of niche products include the concept of fair trading, which has been lobbied for effectively and gained ground in recent years in developed countries, especially for food and beverage items from tropical developing countries. Concerns about issues such as sustainable resource management, special problems related to international commodity trade and markets and linkages with "poverty reduction strategies"[21] have been articulated by Christian Aid[22] in their *Global Supermarket Report* (1996), in the Oxfam Report (Watkins, op. Cit), the *World Development Movement* in their *"People before profits"* campaign. Furthermore, the *Max Havelaar Foundation* and fair-trade organizations have promoted the concept of fair-trade. This is now becoming a significant issue for business, particularly retail corporations marketing goods identifiable as "Third World" products. Here again, the acceptance of fair trade principles by large traders and supermarkets will be crucial for the impact to be felt by a large number of producers.

## VI. OPPORTUNITIES ARISING FROM ORGANIC PRODUCTS

### A. Actual versus perceived market opportunities in developed countries

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21 See Watkins, K. *"The Oxfam Poverty Report"*, Oxfam, Oxford, 1995.

22 See Christian Aid, *"The Global Supermarket"*, Christian Aid, London, 1996.

32. A review by the International Trade Centre (WTO/UNCTAD)[23] indicates that in most developed countries the market share for organic agricultural products is 1 to 2 per cent or less, but rising rapidly. In some smaller countries, such as Austria, Denmark and Switzerland, market shares are already between 2 and 3 per cent. According to the ITC study, in several markets, demand is growing at 25 to 30 percent per annum. However, despite this quick expansion, it is as yet unclear, whether organic products can surpass the benchmark of some 10 or 15 per cent of total market size, thus graduating from niche markets.

33. This raises the question of perceived versus real market opportunities for developing country producers. Rapid demand growth for organic food in developed countries is most likely creating temporary supply-demand gaps, of significant magnitude at times, that can be bridged by supply from developing countries. Such short-term opportunities can, however, only be seized if certification requirements in export markets can be met and market access is facilitated. As long as developing country producers retain significant production cost advantages, based on lower labour costs or natural production factors (such as a longer vegetation period that allows several harvests), they might be able to consolidate market shares gained in the short-term.

34. In the medium-term, organic production capacity in developed countries is likely to expand rapidly, spurred by attractive prices and subsidies by various Governments.[24] The long-term effects of projected increases in organic production in developed countries on market prices and import levels are uncertain. Furthermore, consumers of organic food are increasingly placing emphasis on food supplied locally. Organic tropical food and beverages, counter-seasonal organic products that compete with Northern supply and high quality organic food appear to provide developing country producers with good opportunities to increase their shares in Northern markets in the medium-and long-term.

### B. Price premiums

35. Generally, price premiums for organic produce reflect higher production and marketing costs related to lower yields, higher post harvest losses, certification costs and higher handling and marketing costs.[25] For example, the cost of organic sugar is significantly higher than the cost of conventional sugar.[26] Even so, such divergent costs need not prevent

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[23] ITC, Organic food and beverages: World supply and major European markets (ITC/P12.E/PMD/MDS/99-VII), Geneva, 1999.

[24] Developed country support measures for organic production are likely to increase significantly, for example within the European Union agri-environmental programmes. In the United States, several States have begun subsidizing conversion to organic farming systems as well as certification. In developing countries, on the contrary, Governments give little support to organic production and hardly provide any subsidies.

[25] Limited retail outlets, higher handling risks, smaller handling and sales volumes, the education of sales assistants and special promotion and information campaigns for consumers all cause additional costs.

[26] One study identifies the following factors leading to cost increases: (a) costs of transitioning areas to organic production; (b) higher labor costs; (c) decline in field yields (ranging from 20 to 60 per cent); (d) decline in mill efficiency (which may be as much as 20 to 30 per cent); (e) extra handling costs to avoid commingling of organic and conventional cane (or beets) as well as sugar; and (f) extra costs related to sanitation requirements for field machinery and mill to maintain the integrity of the organic product. On the other hand, there will be reduced input costs. In the case of Brazil, high price premiums are reported, compensating for lower yields (organic sugar yields are estimated to average 70 tons of cane per hectare compared with 85 tons for conventionally grown cane). The export market price is three times the price for conventional sugar. For the domestic market, the organic sugar now being sold in Brazilian supermarkets costs a reported five times that for conventional sugar. Peter J. Buzzanell

producers and marketing agents from realizing higher profits, based on price premiums of organic produce at retail level. As is the case for most other commodities, the share of producer prices in retail prices of organic products hardly surpasses 10 to 20 per cent. Therefore, even significantly higher production costs can theoretically be compensated for by moderate price premiums at retail level, provided that marketing agents (e.g. importers, wholesalers and retailers) do not entirely, or mostly, appropriate the extra income.

36. When attempting to answer the question whether organic products[27] are more expensive than conventional ones in real terms, it must be borne in mind that generally food prices do not internalize environmental and health costs of conventional production, processing and handling methods. Such significant social and environmental costs are among other things caused by soil erosion, excessive water use and contamination as well as the environmental and occupational impact of agro-chemical use. If such costs were partly or entirely internalized, production and processing costs of organic produce would remain significantly below those of conventional products. Price premiums may fall when production increases. In the long run, this may be countered by policies that lead to greater internalization of environmental costs.

37. In each OECD market and for each of the major product groups, a few specialised organic traders tend to dominate imports.[28] This market structure carries the risk that price premiums at retail level are to a significant extent appropriated by few marketing companies.[29] Stringent certification requirements and the role of certain environmental labels in this regard might reinforce the bargaining position of the key marketing companies. This explains the interest, both of producers and consumers, in the use of fair trade schemes for enhancing the production, export and marketing of organic produce at fair producer prices. UNCTAD field studies in India, for instance, show that a substantial number of small producers do not obtain market premiums for growing organic spices; they have to sell their produce in non-organic markets. Furthermore, price premiums significantly differ between products. Retail premiums for spices, for instance, generally do not increase by over 5 per cent, whereas price premiums for high quality tea have been as high as 1000 per cent.[30]

38. Organic agriculture offers multiple benefits beyond export promotion. This concerns natural resource conservation, food security and sustainable rural development. The rehabilitation of soil fertility through organic management and diversified cultivation of traditional food can increase farming systems resilience, improve household nutrition and

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(Executive Director, Peter Buzzanell & Associates, Inc.) Organic Sugar: Short Term Fad or Long Term Growth Opportunity? For the International Sugar Organization, 9th International Seminar "Hot Issues for Sugar" November 21, 2000, London, United Kingdom.

27 It also needs to be noted that production cost estimates for organic produce conceptually often differ from that of conventional food products in that organic production has no single crop focus. Organic farm systems are based on rotation of several crops, on which production costs are distributed depending on many local peculiarities of crop management, crop selection and ripening periods.

28 ITC, op. cit. and M. Buley, An overview on the European market with special emphasis on Germany, paper presented at Export Seminars on Export Development of Organic Food and Beverages in Asia, ITC, 14 September 2000.

29 It appears that large exporters with well established marketing channels are able to catch significant price premiums. No information is available, however, on price premiums available for the numerous small farmers working with large exporters/importers or for small companies exporting through other channels.

30 Some producers and retailers may, at times, prefer selling excessive supply in ordinary markets to avoid an erosion of price premiums in niche markets.

decrease dependence on single crops for volatile markets. One of the key challenges for developing country Governments is to develop organic agricultural policies that combine income generation with improved domestic food production. The latter involves raising productivity of poorly endowed areas by maximizing the use of local resources. Such policies would better respond to self-reliance, local food needs and health of resource-poor farmers. Also, by generating additional employment, organic agriculture can check rising migration to urban areas.[31] Experience shows that farmers both in developed and developing countries are aware of the environmental, occupational and health improvements that organic production can generate[32], but their main motivation is still improved income in the short-term,[33] rather than concern about the environment in the longer term. This explains the key role of price premiums.

## VII. STEPS REQUIRED TO ENHANCE PRODUCTION AND EXPORT CAPACITIES

### A. General measures

39. Several measures could be considered in order to alleviate the constraints to developing countries' production and exports of agriculture and food products. Governments of exporting and importing countries as well as the international community have roles to play in this respect, particularly in providing a supportive environment for the enterprise sector, which needs to adapt its business strategies to new market realities. The measures include: (i) access to high quality inputs such as improved seeds; (ii) enhancement of information flows; (iii) improved access to financing, particularly for small producers; (iv) harmonization of standards; (v) support to marketing efforts; and (vi) the building of partnerships and associative structures both within and across countries.

40. In many developing countries, particularly LDCs, small producers have difficulty to obtain high quality seeds, as well as technical advice on improved production methods. Apart from the physical availability of the inputs, expanded extension services, which have recently been curtailed due to budgetary constraints, are crucial.

41. Improved access to market intelligence and to information about standards and quality requirements would considerably improve the possibilities of developing country producers, particularly small producers, to target markets and take steps to make their products conform

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[31] N. Scialabba, FAO secretariat, Factors influencing organic agriculture policies with a focus on developing countries, paper presented at IFOAM 2000 Scientific Conference, Basel, 28-31 August 2000.

[32] Apart from price premiums, tea producers in India interviewed by UNCTAD provided the following reasons for converting to organic production: (i) agriculture extension services provide small initial loans; (ii) over time (6-8 years), farmers see an increase in productivity and a reduction in production costs (e.g. organic pepper plants need to be replanted every 15-20 years only, whereas non-organic ones have to be replanted every 6 years); (iii) group certification has reduced certification costs; and (iv) assurance of a fixed price and market instead of uncertainties associated with auctions.

[33] Improved income does not only result from price premiums, but also from reduced production costs. As demonstrated by organic coffee growers in Costa Rica and organic maize producers in Kenya, stable yields, based on improved soil fertility, in combination with lower input costs (including water) outperformed conventional agriculture over the medium-term (for Costa Rica, see: Reuters News Service, 10 April 2001, quoted at: www.planetark.org/dailynewsstory; for Kenya, see: N. Scialabba, op.cit. p. 10).

to formal and informal requirements. Intergovernmental organizations including UNCTAD clearly have an important role to play in this area.

42. Lack of access to credit is a major problem for developing country producers. The risks inherent in production and marketing of agricultural products constrain access to conventional commercial credits while the use of financing and risk management methods adapted to the specific characteristics of agricultural production may encounter obstacles in national legislation. Moreover, knowledge about structured finance and commodity price risk management is often limited both in the public and private sector in developing countries. Facilitation of the use of such techniques, including through legislative changes, technical assistance and training are all needed to enable producers to reduce financing costs and remove this obstacle to expansion.

43. As already mentioned, the harmonization of quality standards, which in any case often have a large degree of overlap, would considerably facilitate the export efforts of developing country producers.

44. The establishment of links to buyers in developed countries can constitute a major investment for developing country producers. There are, however, several ways of reducing the costs through partnerships, either between producers in the form of national or regional industry/exporters' associations or between producers and buyers, for instance, through agreements with supermarket chains. In the latter case, developing country producers would improve their bargaining position by negotiating collectively with the buyers.

### B. Measures related to niche products, in particular organic food and beverages

45. There are several short- and medium-term measures developing countries should consider for profiting from enhanced production and export opportunities: (i) awareness-raising; (ii) research and market studies; (iii) facilitating certification and reducing its costs; (iv) developing national standards; (v) developing local markets; and (vi) providing appropriate governmental and technical support.

46. There is a need to increase awareness of the trading opportunities for organic products as well as the environmental, economic and social benefits of organic production. Awareness raising is also essential to help develop a domestic market for organic products. NGOs can play a key role, in particular in awareness raising among consumers and smallholder producers.

47. Further research and development is needed to promote organic farming in developing countries. For example, there is a need to identify or develop new varieties of plants resistant to pest and diseases and capable of producing higher yields. Other areas of research to be encouraged include biological pest reduction methods, the development of agricultural processes tailored to local conditions, the use of by-products and development of high-value organic products.[34] There is also the need for more market research, including on price premiums and the conditions under which they accrue to producers/exporters. Marketing strategies need to be investigated and opportunities for e-commerce evaluated.

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[34] The World Bank, Regional Development Banks and the Common Fund for Commodities could be instrumental in this regard.

Furthermore, it is worth studying the use of brand names or geographical indications to differentiate products, in particular in export markets.

48. The high cost of certification is a major impediment to increasing certified agricultural production in developing countries. Several steps, including the following, could be taken to reduce such costs:

- Assistance from donors and cost-sharing with developed country partners, for example in the framework of fair trade or development projects;
- Training of local inspectors and other personnel to work with an international certification body operation in a particular developing country;
- Development of a national, Government-supported certification system, with the assistance of IFOAM or bilateral/multilateral donors;
- International accreditation of national certification bodies, for example by IFOAM's International Organic Accreditation Service (IOAS), and competent authorities in major importing countries;
- Negotiation of equivalency agreements, including, for example, recognition under European Union Regulation 2092/91;
- Flexible mechanisms to make certification more affordable for small producers, such as "umbrella certification" (e.g. certification of entire geographical areas or groups of producers rather than individual enterprises);
- Provision of special assistance for certification in LDCs;
- Regional cooperation on the development of standards, certification methods and certification organizations.

49. The development of national standards can provide a broad framework for the promotion of organic agriculture and form the basis for certification agencies. They are particularly important for large producing and exporting developing countries.[35]

50. Currently most developing country Governments provide little or no support for organic agriculture. There is, however, much that could be done. For example, agricultural policies and regulations could include special incentives for organic production, such as tax relief or low interest loans. Agricultural extension services and producer organizations could assist in conversion to organic methods. Governments can also assist in overseas marketing and sales and the provision of information. In India, for example, the "National Programme for Organic Production" (NPOP) was established to provide an institutional mechanism for production and export of organic food products, taking into account requirements of international markets.

51. The development of local markets may allow economies of scale. A strong local market is also necessary to export with variety and quality. Governments can support domestic market growth in several ways, including educating consumers and holding organic product fairs/markets. In order to develop local markets and to raise local consumer awareness, the promotion of concepts such as "Low External Input Sustainable Agriculture"

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[35] Without active Government support, the export of certified organic products risks becoming a business that only large farmers, or highly organized groups of small holders can afford. Although there is an IFOAM Accreditation Criteria Programme for Small Holders Certification, there is no general agreement on how inspection and certification of small holders should be organized. This often implies high costs to producers and hence export difficulties for developing countries. N. Scialabba, op.cit.

in South India, "safe vegetables" in Viet Nam or "green food" in China can be useful instruments.

52. Factors which normally constitute disadvantages, such as the small size of markets for Environmentally Preferable Products (EPPs) and the dependence on donor support may actually work in favour of LDCs. Indeed, producing for niche markets may be one of the few options for LDCs to diversify exports toward value-added products.

53. Importing countries could implement the following measures to promote imports of organic products from developing countries:

- Market information: Developed countries' Governments and Import Promotion Agencies could facilitate the provision of information on organic standards and regulations, market opportunities and other relevant factors to exporters from developing countries;
- Technical assistance: Multilateral and bilateral donors, as well as Import Promotion Agencies could increase technical assistance to developing countries with a potential to produce and export organic products;
- Easier market access: Less complicated requirements and procedures are needed. This includes improved application of the concept of equivalence. Furthermore, organic standards and conformity requirements should not discriminate against imports. Governments and organic standardization bodies should also comply with the provisions of the WTO Agreement on Technical Barriers to Trade;
- Increase quota amounts under tariff quota systems: The Harmonized System nomenclature does not currently contain specific tariff lines for organic products. However, within the system of tariff quotas, organic products may be entered under specific categories of quotas subject to low tariffs;[36]
- Trademarks: Developing countries could seek to obtain trademarks for certain categories of organic products. Although as yet an unresolved trade issue, the extension of geographical indications to a number of organic products may offer opportunities for expanding markets for high-quality products and obtaining higher price premiums;
- Non-trade concerns: Organic farming can enable smallholders in developing countries to attain household food security and modest income while regenerating the land, regaining biodiversity and supplying quality food to local communities.[37] It could be worth considering to what extent such arguments justify domestic support measures in developing countries, under article XX of the WTO Agreement on Agriculture;
- Partnerships and product stewardship: International business partnerships and public-private partnerships by supermarkets as well as fair trade and similar organizations along the supply chain should be encouraged and supported by developed countries;
- Support measures: Increasing support measures for organic production in developed countries may render the implementation of commitments concerning the reduction of domestic support less transparent. They may also introduce elements of unfair competition in niche markets for organic products. Such issues may require attention in the WTO context.

## VIII. POSSIBLE ISSUES FOR DISCUSSION BY EXPERTS

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[36] Recently, the United States Department of Agriculture (USDA) raised the specialty sugar quota, in large part to accommodate the growth in organic sugar demand in the United States.

[37] For more information, see: Angelina M. Briones, op.cit.

54 Experts could address the following issues:

**Market access**

- What have been the main barriers to entering international markets for food products? Do the nature of barriers differ in developed and developing countries? What can be done to eliminate these barriers? What can be done to respond to them?
- Have tariff preferences, e.g. for ACP countries, been an important factor for export success?

**Market entry**

- How important are market information needs in the context of enhancing production and export capacities for food products? How can access to such information be improved for enterprises that are not linked to international firms? Can cooperative arrangements among exporters help in this respect? What should Governments do?
- Have international retailing firms, such as supermarket chains, provided significant opportunities for entering import markets? Are there any major problems related to contractual and other links with supermarket chains and vertically integrated international food companies? Would trade liberalization in importing countries significantly improve the contribution of large international firms to exports of developing countries?
- Do experts see significant opportunities for direct sales by exporting countries' firms? Is it possible for these firms to compete effectively with large multinational companies and purchasing concerns in developed countries? Would cooperative arrangements among exporters provide a significant boost?
- Do developing countries have scope for establishing brand names or differentiating their products in important markets? If so, how can this be done most effectively?

**Standards and quality**

- Does the existence of multiple standards place developing country producers and exporters at a disadvantage? What can be done in this respect (mutual recognition, harmonization, improved information, SPS and TBT agreements)?
- Is there a desirability and practical scope for streamlining the different standards such as ISO 9000, ISO 14000 and HACCP? Would this help developing countries or be a disadvantage?
- What are the main technical cooperation requirements for complying with quality standards and establishing the requisite managerial competence? Could one envisage the establishment of a fund for this purpose to be co-financed by Governments and private sector (of developed and developing countries)?

**Niche products**

- Which organic and other niche products are the most attractive candidates for production and export by developing countries? What are the factors contributing to successful promotion of organic agriculture?
- Are there relevant national experiences on measures taken to enhance production and export opportunities for organic products, including, in particular, awareness-raising,

research and market studies, facilitating certification and reducing its costs, developing national standards, developing local markets, and providing appropriate Government and technical support?

**Strategies**

- What is the optimal division of labour between Governments and the private sector, in terms of upgrading and ensuring quality?
- What are the practicable avenues for implementing special measures by importing countries aimed at promoting imports of organic products from developing countries (equivalency, recognition of IFOAM accreditation, increased quota amounts under tariff quota systems, granting of tariff preferences for organic products, or international partnerships and product stewardship)?
- What are the national experiences, if any, with regard to national strategies on facilitating production and export of organic products (e.g. on awareness raising, promoting research and development, facilitating certification, development of national standards, creation and expansion of local markets)?
- What can be expected of UNCTAD, together with ITC and other relevant international organizations, in terms of:
  - providing information, research, analysis and policy advice (market information, better understanding of value chains, product differentiation, others),
  - ensuring transparency as well as harmonization and compatibility of standards and quality requirements,
  - technical cooperation activities and specifically as regards organic products, the possible extension of ongoing country projects by the UNEP-UNCTAD Capacity Building Task Force (CBTF) on Trade, Environment and Development, and the linking of work on harnessing traditional knowledge for development and trade to technical assistance on enhancing production and export capacity of EPPs in developing countries;
  - regional cooperation, including among LDCs, on EPPs,
  - upgrading enterprise strategies and government policies,
  - improving domestic structured finance infrastructure?